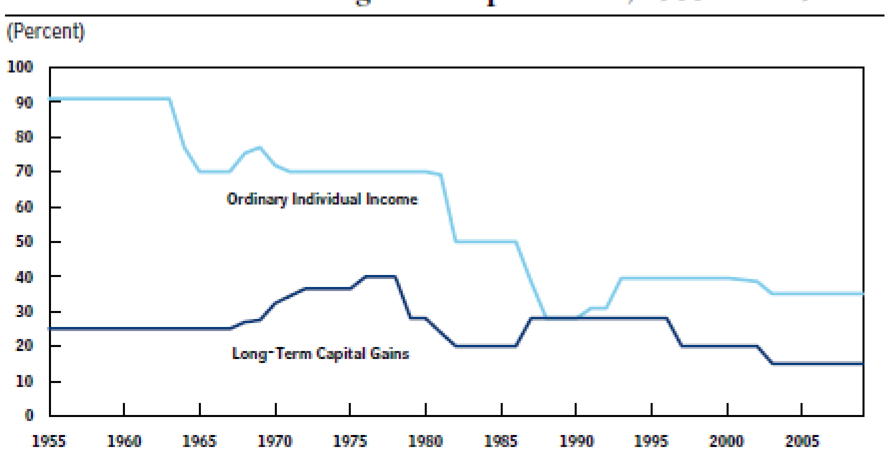
Tax income from wealth at the same rate as income from work: $918 billion over 10 years

The Idea: Currently, profits from the sale of stocks, bonds, real estate, and other assets – also known as capital gains – can only be taxed at 15 percent on every dollar, while the highest tax rate for wages is 35 percent. If capital gains were taxed at the same rate as wages and salaries, the country could raise roughly $918 billion[1] over the next 10 years.

The Rationale: Between the establishment of the federal income tax in 1913 and 1921, the government taxed income from wealth at the same rate as earned income. In 1918, the highest tax rate was at 77 percent for all income, regardless of source. However, in 1922, the government began taxing income from wealth at a lower level than earned income, reducing the top wealth tax rate to 12.5 percent. In the early 1940s, the capital gains tax rate was raised to 25 percent, and in the 1970s, the top rate went up to 39.9 percent. Then Congress began cutting the rates. In the 1980s, in Ronald Reagan's second term, income and wealth were both taxed at 28 percent; President Clinton reduced the capital gains rate to 20 percent, and George W. Bush reduced the capital gains tax rate to the exceptionally low level of 15 percent, almost to its 1922 rate when the bulk of federal tax receipts came from excise taxes.

Maximum Statutory Marginal Income Tax Rates on Ordinary Individual Income and Long-Term Capital Gains, 1955 to 2009



Sources: Department of the Treasury, Internal Revenue Service and Office of Tax Analysis.

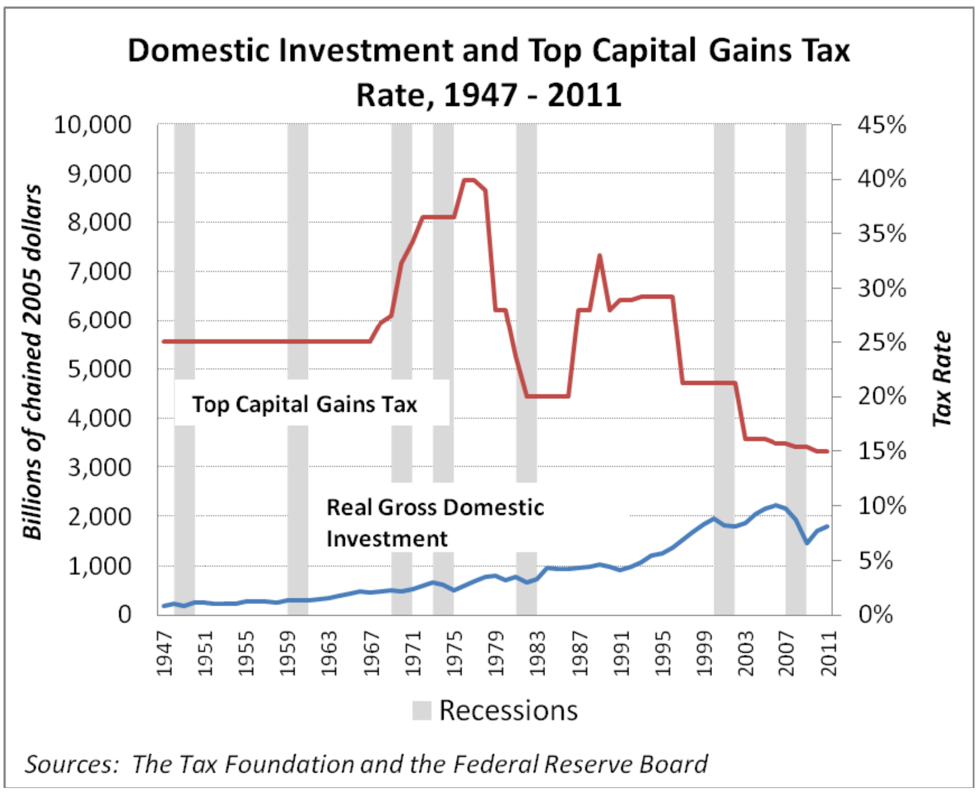
1742 Connecticut Ave. NW
Washington, DC 20009

tel: 202.234.8494
fax: 202-234.8584

email: ombwatch@ombwatch.org
web: http://www.ombwatch.org

Proponents of raising the capital gains tax argue that it would increase fairness: why should someone earning $100,000 in salary pay more taxes than someone receiving $100,000 in stock dividends? And since it is the wealthy who disproportionately rely on income from stocks and bonds, a low capital gains tax rate means lower-income people are paying more in taxes than higher-income individuals.

Those who want to keep lower taxes on the profits from trading argue that lower taxes on investors increases investment dollars and will stimulate the economy. However, as the following graph (and other evidence) shows, there is little correlation between domestic investment and low tax rates on capital gains. Real domestic investment had been growing steadily when the capital gains tax was at 39.9 percent and fell during the period when the rate was 15 percent.



Support for the idea: Recent polls show a majority of the public approves of taxing capital gains as ordinary income. Warren Buffet, one of the wealthiest men on the planet, who makes his fortune from capital gains, has famously said that his tax rate should not be lower than his secretary's. President Obama would raise the capital gains rate back to 20 percent. However, neither has called for taxing capital gains at parity with earnings.

Of the plans reviewed for this revenue project, the following support raising capital gains tax rates: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step* and *Budgeting for Growth*, Andy Stern's *21st Century Plan*, the Institute for America's Future *Citizens' Commission*, the National Commission on Fiscal Responsibility's *Moment of Truth*, Rep. Jan Schakowsky's *Deficit Reduction Plan*, Steven Peralstein's *Deficit Reduction Op-Ed*, Joseph Stiglitz's *Principles and Guidelines for Deficit Reduction*, Citizens for Tax Justice's *Policy Options*, Comeback America's *Restoring Fiscal Sanity*, the Congressional Progressive Caucus' *People's Budget*, the Bipartisan Policy Center's *Restoring America's Future*, and the Congressional Black Caucus' *The Responsible Path*.

[1] *Investing in America's Economy*, Our Fiscal Security, pg. 31-2.